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No. 426

IN THE

Supreme Court of the United States

OCTOBER TERM, 1948.

WORLD PUBLISHING COMPANY, A CORPORATION, *Petitioner*,

v.

UNITED STATES OF AMERICA, *Respondent*.

REPLY BRIEF IN SUPPORT OF PETITION FOR CERTIORARI.

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The government rests its case on the proposition that only questions of fact are involved.

There is no dispute however as to the facts. They require, on a correct interpretation of the law, judgment for the petitioner.

The law, for the purpose of determining the good faith of taxpayers in the accumulation of surplus, provides the test as to whether in effect the accumulation is necessary and proper in the operation of the business. The case hinges on the meaning of the statute.

In *M'Culloch* v. *Maryland*, 4 Wheat. 316, 4 L. Ed. 579, for nine days the Supreme Court listened to arguments by

the most distinguished lawyers of the age, Webster, Pinkney, Luther Martin and others, primarily on the question as to the meaning of the words "necessary and proper" in the constitution—not as a question of fact, but as a question of law.

In his decision, Chief Justice Marshall says (pp. 413, 414):

> "But the argument on which most reliance is placed, is drawn from the peculiar language of this clause. Congress is not empowered by it to make all laws, which may have relation to the powers conferred on the government, but such only as may be 'necessary and proper' for carrying them into execution. The word 'necessary' is considered as controlling the whole sentence, and as limiting the right to pass laws for the execution of the granted powers, to such as are indispensible, and without which the power would be nugatory. That is excludes the choice of means, and leaves to Congress, in each case, that only which is most direct and simple.
>
> "Is it true that this is the sense in which the word 'necessary' is always used? Does it always import an absolute physical necessity, so strong that one thing, to which another may be termed necessary, cannot exist without that other? We think it does not. * * * To employ the means necessary to an end, is generally understood as employing any means calculated to produce the end, and not as being confined to those single means, without which the end would be entirely unattainable. * * * Almost all compositions contain words, which, taken in their rigorous sense, would convey a meaning different from that which is obviously intended. It is essential to just construction, that many words which import something excessive should be understood in a more mitigated sense—in that sense which common usage justifies. The word 'necessary' is of this description. It has not a fixed character peculiar to itself. It admits of all degrees of comparison; and is often connected with other words, which increase or diminish the impression the mind receives of the urgency it imports. A thing may be necessary, very necessary absolutely or indispensably necessary. To no mind would the same idea be

> conveyed by these several phrases. * * * This word, then like others, is used in various senses; and, in its construction, the subject, the context, the intention of the person using them, are all to be taken into view."

The mere fact that the courts of Maryland, from which the appeal was taken, had found the creation of a national bank not to be necessary under the Constitution, did not suffice to convert the question into a mere question of fact.

Again, in the *Legal Tender Cases,* 12 Wall. 457, 20 L. Ed. 287, the interpretation of the words "necessary and proper" was before the court. Without regard to the factual decision of the lower court on what was necessary, the Supreme Court proceeded to the construction of the words of the Constitution. Said the Court at page 531:

> "Nor can it be questioned that, when investigating the nature and extent of the powers conferred by the Constitution upon Congress, it is indispensable to keep in view the objects for which those powers were granted. This is a universal rule of construction applied alike to statutes, wills, contracts and constitutions. If the general purpose of the instrument is ascertained, the language of its provisions must be construed with reference to that purpose and so as to subserve it. In no other way can the intent of the framers of the instrument be discovered."

Using the appropriate canons of construction, the following appears in this case.

The "reasonable needs of the business" provision of the statute is prescribed as a test for determining the good faith of taxpayers. As such it requires a liberal interpretation. Bad faith cannot be imputed (as did the lower court) from a mere difference of opinion on business needs nor from the fact that the majority of the court might have voted differently than did the board of directors.

The need of the business for the accumulation is so clear in this case that only an erroneous construction of the law could result in a contrary conclusion.

As the revenue agent who initiated this penalty said (Ex. 1, R. 120, 129): "The need for the new presses appears to be real and it is the examiner's opinion that they will be installed as soon as practicable after termination of the war. * * * But as of December 31, 1942 there was no reason to anticipate an early cessation of hostilities and the convenient loosening of war time priorities. The corporation's management therefore at the close of the year 1942 would have no reasonable hope that the desired new equipment could be purchased in the immediate future."

That this was the real basis, not only of the revenue agent's decision but of both lower courts', is irrefutably clear on the face of the record. That it involves a rigid and improper interpretation of the statute is certain in the light of the purpose of the "reasonable needs of business" provision.

The acid test of the court's decision is found in the fact that the accumulation was so clearly needed that the chief judge in his dissent said it was "obvious" and was the exercise of "ordinary business prudence". How can an accumulation so viewed by one of the impartiality and ability of Judge Phillips be deemed an earmark of bad faith?

The answer is clear—; only by a misinterpretation of the statute.

The revenue agents and the lower courts in this case have construed the "reasonable needs of the business" provision of the statute as meaning the immediate and indispensable needs. Says the court and government in its brief, page 7, "There can be no doubt that there was a reasonable, though not acute, need for a new press", etc. Thus, the operation of a broadcasting station is not indispensable to a newspaper and so is excluded by the court as a reasonable need. The fact that it is so appropriate as to be commonly availed of by the leading papers of the country is not enough. It isn't "absolutely" necessary—nor indispensably necessary,

and so, is not under the court's interpretation a reasonable need.

The adherence of the government and the majority of the court to an extreme interpretation of the language of the statute also appears in amazing insistence on measuring need by the admittedly inadequate minimum estimated cost of $500,000. With an actual undisputed contract base cost before it of $938,000 (with an escalation clause in addition) the court never budges from its $500,000 standard. The necessity for this adherence is found in the fact that the total surplus including everything not only real estate, but all of the quick assets was far less at the end of both the crucial years than the actual minimum base contract price of the necessary equipment and building.*

The meaning of the word "necessary" has been frequently passed on by the courts in construing the provision of the statute permitting deductions of "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business". The Supreme Court in its definition of the word "necessary" in that provision of the revenue laws, has followed the meaning given it by Chief Justice Marshall in *M'Culloch* v. *Maryland, supra,* namely "appropriate and helpful".

The importance of Supreme Court definition in that instance for the proper administration of the revenue laws, is evident from an examination of Shepard's Citator and the C.C.H. Citator Table showing repeated reference by the courts and reliance by the Bureau of Internal Revenue in its rulings on the Supreme Court definition. *Welch* v. *Helvering,* 290 U. S. 111. See, *Deputy* v. *DuPont,* 308 U. S.

* There is a possible ambiguity and confusion on page 11 of the government's brief. The $427,287.39 referred to, was actually a part of, and included in, the $562,521.98 surplus of Dec. 31, 1941, and was not in addition thereto. The total surplus at the end of years 1942 and 1943 was $643,062.26 and $732,626.47 respectively (Ex. B, p. 27, Stipulated Facts). The market value was below the book value (Ex. E and F, pp. 33, 35, Stipulated Facts).

488; *Commissioner of Internal Revenue* v. *Heininger*, 320 U. S. 467; *Cornhauser* v. *United States*, 276 U. S. 145.

For the use of the *Welch case* by the Bureau of Internal Revenue in its instructions to collectors and taxpayers, see G.C.M. 24,227; 1944 CB 93 IT 3732, 1945 CB 88 IT 3412, 1940-2 CB 174 IT 2888, XIV-1 CB 54.

Yet the limitation upon industrial progress imposed by rigid, contradictory and uncertain definition and application of the "reasonable needs" provision of the statute here involved, is of greater importance to the country and the Treasury than was the question in the *Welch case*.

LATEST TAX COURT DECISION.

J. L. Goodman Furniture Co. v. Commissioner, 11 Tax Court 64 (Sept. 30, 1948)

(The advance sheets of this case were received after our application for certiorari was filed)

This case involves accumulation during 1942 and 1943 for the erection of a branch store and expansion after the war. The store site was not bought until 1947.

The Commissioner followed the line of the lower court decisions in the *World Publishing case*. Said the Tax Court (p. 5), "He argues that it had no 'immediate' need for so large a surplus". The accumulation was upheld by the Tax Court, however, as a reasonable business need despite the long necessary delay in expenditure. "The retention of that additional capital was justified by the boom anticipated at the end of the war which would be enjoyed by the existing store despite its location".

Until the Supreme Court acts, this contest between the Treasury and the Tax Court and between the various cir-

cuits as to whether the statute requires that the need be immediate and acute, will continue.

Respectfully submitted,

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